

## **FACT SHEET**

### **FOURTH JOINT STATUS REPORT UNDER THE U.S.-JAPAN ENHANCED INITIATIVE ON DEREGULATION AND COMPETITION POLICY**

**June 30, 2001**

#### **OVERVIEW**

The Fourth Joint Status Report under the Enhanced Initiative on Deregulation and Competition Policy (Enhanced Initiative) details important deregulatory steps Japan will take to help its economy grow and increase access to Japanese markets for U.S. businesses and workers. It contains measures in key sectors and structural areas, including telecommunications, information technology, energy, housing, medical devices and pharmaceuticals, financial services, competition policy, Commercial Code reform, legal reform, distribution, and transparency.

These measures represent important progress in Japan's ongoing efforts to streamline and reduce the myriad regulations that have contributed to limiting its ability to return to sustainable growth.

Implementation of the measures will benefit Japanese consumers by helping to reduce prices, increase choice and encourage the introduction of more innovative goods and services. Simultaneously, by creating a less burdensome regulatory environment in Japan, the Enhanced Initiative is expanding opportunities for U.S. firms exporting their goods to Japan and investing there.

Building on the progress achieved under the Enhanced Initiative, the two governments will continue their bilateral focus on economic reforms aimed at helping Japan return to growth while at the same time opening markets through the U.S.-Japan Regulatory Reform and Competition Policy Initiative, a key component of the U.S.-Japan Economic Partnership for Growth, which was launched by President Bush and Prime Minister Koizumi at a Camp David summit on June 30, 2001.

## **TELECOMMUNICATIONS**

**Background:** The inability of competitive telecommunications carriers in Japan to dislodge NTT from its control of 99 percent of subscriber lines and 60 percent of mobile customers has hampered Japanese consumer access to innovative, low-cost services, particularly relating to fixed line Internet access. This in turn has restricted growth and investment in Japan's \$130 billion telecommunications market, the world's second largest. NTT's advantage as an incumbent supplier with control over "bottleneck" facilities and a government regulatory regime that has supported this dominance have hindered the ability of new entrants' to exploit their competitive advantages in innovation, responsiveness, and efficiency.

**Accomplishments:** To address these problems Japan will:

- Vigorously apply and enforce "dominant carrier regulation" measures enacted by the Diet on June 15, 2001. These regulations will strengthen safeguards to prevent NTT from discriminating against competitors. They will also ensure that competitors gain access to NTT's optical fiber, rights of way, switching offices, and other facilities, and that the dominant wireless carrier, DoCoMo, provides cost-based interconnection.
- Develop guidelines for competition to ensure that entry by NTT East and West into Internet or other services is conditioned upon satisfying pro-competitive conditions.
- Ease the regulatory burden facing new entrants in filing tariffs and contracts by shifting to a notification, rather than an approval system for such filings.
- Ensure cost-based access to NTT's fiber optic cables and access to wholesale rates for services provided by NTT. This would permit new entrants to roll out competitive services more quickly based on a discount of NTT retail services.
- Ensure the fair, non-discriminatory and transparent provision of access to rights of way for carriers, facilitating their ability to build out their networks.
- Ensure that any universal service funding mechanism is limited to basic voice services, open to competitors, and based on a cost model reflecting an efficient operator.
- Continue to reduce interconnection rates, improve the existing cost model, and in the case of mobile interconnection, ensure that tariffs for NTT DoCoMo are publicly disclosed and reflect the costs of an efficient operator.

**Benefits to the U.S.:** These steps will significantly improve opportunities for access by U.S. firms to Japan's telecommunications sector. Specifically, it will begin to rebalance the overwhelming advantages NTT has had in maintaining its monopoly in favor of new entrants, who have invested billions of dollars in new networks but have had little success in capturing significant market share from NTT. The additional flexibility new entrants will gain in quickly introducing new services should accelerate innovation and price competition which is essential to stimulating overall growth in the information technology sector.

## **INFORMATION TECHNOLOGY**

**Background:** Japan has recently embarked on an ambitious plan to become a global leader in information technologies, which includes a commitment to revise laws for the digital age that will further facilitate e-commerce (including e-business and e-government). Even so, development of the Internet and e-commerce is lagging in Japan when compared to other developed countries. As Japan responds to the challenges that lie ahead in this pivotal sector, the U.S. Government is working with Japan to promote a thriving IT sector.

**Accomplishments:** To further promote the growth of its IT sector, Japan will:

- Continue discussions with the U.S. Government to facilitate legislation in Japan that will provide clear-cut Internet Service Provider liability rules.
- Work towards strengthening the protection of intellectual property rights on the Internet by supporting the entry into force of the WIPO Performances and Phonograms Treaty (WPPT), which would protect copyrighted works and music online; and by continuing discussions with the U.S. Government on the treatment of temporary copies.
- Ensure that Japan's privacy legislation supports a self-regulatory framework, including self-regulatory dispute mechanisms.
- Continue to consider amending existing laws and regulations which hinder the development of e-commerce, in order to facilitate paperless transactions.
- Promote electronic government procurement by creating a consolidated database of government procurement information and introducing electronic bidding for public works projects.
- Work closely with the U.S. Government on information and network security issues.

**Benefits to the U.S.:** These measures will promote a regulatory environment for e-commerce which is private-sector led and which will help improve intellectual property protection on the Internet in Japan. They will also promote the growth and development of the IT products and services market in Japan. Expected to reach nearly \$136 billion by the end of 2004, this market will provide significant opportunities for U.S. firms and their leading technology products.

## **MEDICAL DEVICES AND PHARMACEUTICALS**

**Background:** Continued over-regulation and inefficiencies in Japan's medical device, pharmaceutical and nutritional supplement sectors have slowed the introduction of innovative, cost-effective products into Japan. Increasing the availability of these products is a key to helping Japan meet the challenge of providing higher quality health care to its aging population while limiting overall costs.

**Accomplishments:** To address these problems, Japan will:

- Implement medical device and pharmaceutical pricing reforms which recognize the value of innovation, encourage the faster introduction and broader availability of innovative products, and will lead to better and more cost-effective treatments for patients.
- Provide a two-month public comment period on the revision of a key component of Japan's pharmaceutical pricing system (i.e. the comparator selection process).
- Improve transparency, speed and consistency of the approval processes for medical devices and pharmaceuticals and publish official documents that clearly outline the procedures.
- Improve the process for accepting foreign clinical data for pharmaceutical approval.
- Take steps to ensure that data requirements of its new system governing the treatment of nutritional supplements (implemented on April 1, 2001) are reasonable and appropriate.

**Benefits to the U.S.:** Japan is the world's second largest market for medical devices and pharmaceuticals. In both sectors, U.S. firms are the dominant worldwide suppliers of innovative products and will be key beneficiaries of the measures Japan has implemented or committed to implement under this year's deregulation package. Although U.S. firms have increased their presence in Japan, their market shares remain lower than the levels they have achieved in other developed countries. The steps Japan has taken and will take are critical to ensuring that the steady stream of innovative medical devices and drugs being developed by U.S. firms can gain timely access to the Japanese market.

## **ENERGY**

**Background:** Japan's energy market is the third largest in the world, following the U.S. and China. Ten utilities collectively meet about 75 percent of Japan's power needs. Japan's March 2000 liberalization of almost one-third of its electricity market, which allows large industrial customers to choose their electricity supplier, was intended to reduce Japan's energy prices, currently the highest in the OECD. Lowering Japan's energy prices through competition would increase economic growth and create new jobs.

**Accomplishments:** Japan has or will take numerous key measures regarding transparency, open access, and market entry intended to ensure the effectiveness of continuing its energy deregulation process, including:

- Promoting open access to Japan's electricity transmission grid by taking steps to ensure transparency and neutrality of wheeling services such as conducting a publicly available audit of utility accounts.
- Fostering fair and transparent treatment of requests by new entrants for transmission capacity expansion by requiring that utilities provide fair and prompt responses to such requests.
- Facilitating new entry and infrastructure development in the electricity and gas markets by conducting a study of existing regulatory requirements for siting new generating plants and transmission lines, and publishing a list of major regulatory requirements for siting new gas pipelines and LNG facilities.
- Fully implementing and enforcing measures designed to ensure fair, open, and non-discriminatory access to Japan's gas transportation services.
- By 2003, conducting and making public evaluations of the progress of electricity and gas market liberalization, including the status of new entry into the market.
- Ensuring that METI works with the JFTC to promote fair and open access to electricity and transmission networks.

**Benefits to U.S.:** U.S. firms will gain access to Japan's \$135 billion electric power market, enabling them to produce, sell and trade energy products and services in Japan's electricity and gas markets. The reform measure listed about will also help generate new opportunities for U.S. firms to export to Japan's \$15 billion market for electrical generation equipment.

## **FINANCIAL SERVICES**

**Background:** Japan's pool of individual savings—valued at over \$12 trillion—is the largest outside the United States. But, until recently, Japanese investors had a very limited range of investment choices, and most of these funds have been held in low-return assets. Strict regulations narrowly defined the scope of financial firm activities, reducing competition and innovation in the sector, as well as limiting the opportunities available to American financial services providers.

**Accomplishments:** Japan's "Big Bang" financial liberalization initiative, which builds on and extends Japan's undertakings in the 1995 U.S.-Japan Financial Services Agreement, commits Japan to a fundamental deregulation of the financial sector. Bilateral financial services discussions have sought to ensure that Big Bang measures were extended and fully implemented, and that foreign firms share fully in the new opportunities opening up. Notable deregulation measures in this report include:

- The effective implementation by the Financial Services Agency of a system of response to written inquiries, including requests for published guidance and no-action letters, and use of public comment procedures by financial authorities and self regulatory organizations (SROs), will improve transparency and regulatory clarity.
- Further liberalization of the financial industry to remove segmentation in banking, insurance, and trust sectors will increase competition among financial service providers, as it has in other financial markets.
- The introduction of defined contribution pension plans (taking effect on October 1, 2001) will provide a wider selection of employee benefit packages to Japanese corporations, pension portability and more options to meet retirement needs to Japanese workers and greater business opportunities to domestic and foreign investment firms.
- The plans to make greater use of information technology in the financial sector -- for disclosure and reporting requirements, and applications and registration procedures -- will increase efficiency, reduce burdens on firms and enhance the overall operating environment.

**Benefits to the U.S.:** Drawing on their technological and innovative strengths, American financial services providers continue to expand on significant commercial opportunities from the liberalization of Japanese financial markets. American firms have also entered the Japanese banking, securities, and insurance sector through the acquisition of Japanese firms. The share of the Tokyo stock market held by foreign institutions and individuals has steadily grown to almost 20 percent, compared with about 5 percent in the late-1980s. American financial services providers are playing increasingly prominent roles as financial advisors in Japan, particularly in areas such as mergers and acquisitions. Opportunities for U.S. firms will continue to expand in the future, as Japanese savers and corporations seek an increasingly sophisticated range of financial products to meet their needs.

## **HOUSING**

**Background:** The Governments of the United States and Japan have worked cooperatively for a number of years to address issues of concern in Japan's housing sector. Japan's \$40 billion home building materials market is the second largest in the world. Numerous restrictions on building size and design and the traditional emphasis on new housing versus maintenance and renovation of existing homes have impeded market access for foreign products and designs, limiting choice for consumers and driving up housing costs.

**Accomplishments:** To address these problems, Japan will:

- Cooperate with the private sector to create a standard appraisal system for resale housing that accurately reflects the value of maintenance and renovation. A new standardized appraisal system will help invigorate the secondary market by providing consumers more comprehensive information on housing choices.
- Remove or significantly limit key financial disincentives associated with the purchase of existing homes, such as permitting longer repayment periods for higher quality resale detached homes and extending the decrease in registration taxes on sales of existing homes from 5 percent to 0.3 percent.
- Announce that our two governments are close to an agreement whereby Japan would recognize the equivalency of the U.S. standards system for grading and certifying wood products.
- Accept that Oriented Strand Board (OSB) is functionally equivalent to plywood.
- Publish and disseminate its test methodology for evaluating fire resistance.
- Review with the United States its implementation of performance-based building codes. We will address concerns about Japan's use of performance criteria and testing methodologies, which impede the use in Japan of building materials commonly used in the United States and elsewhere.

**Benefits to the U.S.:** These reforms are intended to help spur Japan's economic growth and provide more affordable, high-quality homes for Japanese consumers. By facilitating the growth of a more vibrant secondary market, these reforms will create important new opportunities for U.S. firms supplying building materials for home renovation and maintenance. The steps to improve equivalency open new opportunities for suppliers of OSB and will improve the competitive position of other U.S. suppliers. The United States expects that reviewing Japan's performance-based building codes will give building material suppliers a better understanding of the standards their products must meet and should lead to the use of a greater variety of U.S. products in Japanese buildings.

## **COMPETITION POLICY**

**Background:** A central goal of the Enhanced Initiative has been to strengthen the role of competition policy and antitrust enforcement in order to eliminate practices and policies that can interfere with an open and efficiently-functioning market in Japan. Of particular concern from an international trade perspective are agreements among manufacturers and groups of distributors to boycott imported products. Bid rigging on government procurements raises questions about the acceptance of competition principles in Japan. The Japan Fair Trade Commission (JFTC) has neither sufficient resources nor the legal tools to be most effective in uncovering and stamping out market-distorting anticompetitive practices. Moreover, the recent Japanese Government reorganization, which placed the JFTC within the same agency that regulates telecommunications and postal services (MPHPT), threatens to undermine the independence and credibility of the JFTC.

**Accomplishments:** Significant new measures to address these problems include:

- Requiring all procuring agencies, at both the central government and local government level, to report suspected bid rigging to the JFTC, to debar bid rigging participants and, where feasible, to claim compensation for overcharges from bid rigging.
- Deciding to strengthen the structure and resources of the JFTC and to review the JFTC's current placement within MPHPT to make its position in the Japanese Government more appropriate for ensuring its independence and neutrality.
- Examining ways to strengthen Antimonopoly Act (AMA) enforcement, including the possible introduction of a corporate leniency program, expansion of the scope of administrative fines and improvement in criminal enforcement procedures.
- Reaffirming that the JFTC will apply the most weighty provisions of the AMA, including administrative fines, against participants of group boycotts.
- Promoting competition in industries that are in the process of deregulation by: preparation by the JFTC of AMA Guidelines for the telecommunications industry; the establishment of a special JFTC Task Force to investigate and take enforcement action against anticompetitive practices in public utility sectors, including telecommunications; and by JFTC and MPHPT (the telecommunications regulator) endeavoring to cooperate.

**Benefits to the U.S.:** Improvement of the competitive environment in Japan will ensure an open market for U.S. goods and services, and will speed needed restructuring of the Japanese economy. Real efforts to eliminate bid rigging will make it easier for U.S. construction and related firms to participate in the huge government procurement market and will send a clear message that the Japanese Government is serious about promoting competition.



## **COMMERCIAL CODE REFORM**

**Background:** Japan's Commercial Code is antiquated by modern standards and imposes a large number of impediments on the ability and flexibility of corporations to raise capital and to govern themselves in ways that encourage efficient business operations and accountability to shareholders. The myriad restrictions in the Commercial Code have impeded the development of capital markets in Japan. These problems have had a detrimental effect on the ability of American companies to invest in Japan and structure and finance themselves in the most efficient manner possible. Japan's current corporate governance system has resulted in a poor allocation of corporate resources, which in turn has impeded restructuring and led to long-term overcapacity problems. And by fostering a system in which shareholders' interests are not adequately addressed, it has insulated corporate management from shareholder and market pressure to operate profitably.

**Accomplishments:** Significant new measures to address these problems include:

- Commencing a major, two-year initiative for widespread reform of Japan's Commercial Code, which has so far resulted in the issuance of an interim report recommending wholesale reduction of restrictions on a variety of corporate financing tools, including the issuance of new shares, stock options, special voting rights for classes of shares, and non-voting shares, as well as improving corporate governance mechanisms.
- Introducing legislation by the end of 2001 that will:
  - ▶ Eliminate significant restrictions on the issuance of stock options by corporations; and
  - ▶ Allow corporations to use electronic means, including the Internet, to provide shareholders with notice of shareholders' meetings and that will allow shareholders to vote electronically.
- Submitting legislation to the Diet in 2002 that will make widespread amendments to the Commercial Code, including a major change of policy that will give companies the option of establishing an executive officer and board of directors committee system instead of having to use the so-called statutory auditor (*kansayaku*) system.
- Publishing or providing other opportunities for the public to review public comments on the interim proposals for Commercial Code reform.

**Benefits to the U.S.:** The Commercial Code reforms, when fully implemented will enable U.S. firms to engage more easily in mergers and acquisitions in Japan, since they will have increased flexibility in financing and corporate structuring options and will be able to use American-style management approaches. The proposed corporate governance reforms will enable U.S. firms operating in Japan to streamline their boards of directors and become more flexible in their oversight. The proposed reforms will also contribute greatly to the creation of a world-class capital market in Japan and to needed restructuring of the Japanese economy.

## **TRANSPARENCY OF THE REGULATORY SYSTEM**

**Background:** Despite improvements in recent years, Japan's regulatory system continues to lack the transparency and accountability necessary to ensure that all players have the same access to government information and the policymaking process. New market entrants and competitors need adequate information on Japan's regulatory system in order to base their decisions on accurate assessments of potential costs, risks and market opportunities. This is especially true for foreign firms, which do not have the same access to the bureaucracy as domestic firms.

### **Accomplishments:**

- Japan is introducing a government-wide "No Action Letter" system. Under the new system, businesses may submit inquiries to ministries and agencies on the interpretation of laws and ordinances and their application to specific factual situations. The ministries and agencies will respond in writing to inquiries generally within 30 days and will make their responses public.
- In April 2001, Japan implemented a government information disclosure law, similar to the U.S. Freedom of Information Act, which for the first time gives the public the right to request the disclosure of information held by Japanese central government agencies. The Japanese Government has also submitted legislation to the Diet that will give the public similar rights to information held by Independent Administrative Institutions (*dokuritsu gyosei hojin*), Public Corporations (*tokushu hojin*), and other corporations.
- Japan has adopted a new policy that requires Japanese ministries and agencies, when introducing new regulations, to examine the need for the regulation, its expected effects, and projected costs, including the burden imposed by the regulation on the public.
- In January 2001, Japan increased regulatory transparency and bureaucratic accountability by introducing a government-wide policy evaluation system.
- Two years ago, Japan introduced a Public Comment Procedure that allows the public to review and comment on draft regulations. The United States, however, has ongoing concerns about the Procedure's implementation, including the lack of transparency after comments are submitted. Japan is requiring its ministries and agencies to make all of the public comments available for review by the public.
- In addition, several Japanese private sector organizations are using, or plan to introduce, the Public Comment Procedure. They are the Japan Securities Dealers Association (JSDA), the Japan Craft Inspection Organization (JCI) and The Investment Trusts Association.

**Benefits to the U.S.:** Reforms that increase the transparency of the regulatory process and make the bureaucracy more accountable help curb onerous discretionary powers of the bureaucracy and shift power to the public. Such reforms also help level the playing field for foreign firms, reducing the special advantages traditionally enjoyed by Japan's domestic firms. For example, Japan's "No Action Letter" system should make the regulatory process more transparent and predictable.

## **LEGAL SERVICES AND LEGAL REFORM**

**Background:** As deregulation and restructuring of the Japanese economy continues, the ability of the business community in Japan to rely on the Japanese legal system to facilitate business transactions and resolve disputes will become increasingly important. Reforms of the Japanese legal system are essential to create a legal environment in Japan that is conducive to international business and investment, that supports deregulation and structural reform, and that meets the needs of both Japanese citizens and the international business community. By continuing to bar Japanese lawyers from becoming partners with foreign lawyers, Japan has limited the ability of Japanese and foreign businesses to obtain the fully integrated transnational legal services they need for efficiently effecting domestic and cross-border transactions.

**Accomplishments:** This year, the Government of Japan has taken significant steps to address the need to modernize and liberalize its legal system:

- Japan established a Judicial Reform Council, which in June 2001 made a number of significant recommendations on reforms needed in Japan's legal system, including:
  - ▶ deregulating the requirements for specified joint enterprises (*tokutei kyodo jigyo*), and studying the restriction that prohibits foreign lawyers from hiring Japanese lawyers (even though Japanese lawyers are allowed to hire foreign lawyers);
  - ▶ increasing the number of legal professionals, including by immediately increasing the number of persons who annually pass the Bar Examination (to 1,500 by 2004) and introducing a new law school system;
  - ▶ increasing the speed and efficiency of civil litigation by reducing by half the length of time required to complete trials; facilitating litigants' collection of evidence at early stages of litigation; and increasing the number of judges;
  - ▶ making the specialized departments concerning intellectual property rights at both the Tokyo and Osaka District Courts function substantially as "patent courts;"
  - ▶ reforming Japan's 100-year-old Arbitration Law; and
  - ▶ undertaking a comprehensive study of judicial oversight over administrative agencies, including review of the Administrative Case Litigation Law.
- Japan has recognized that the demand for international legal services has significantly increased in Japan and the importance of promoting and facilitating further cooperation and collaboration between Japanese and foreign lawyers. To that end, Japan will continue to exchange views with the Foreign Lawyers' Association of Japan and the American Chamber of Commerce in Japan.

**Benefits to the U.S.:** Japan's recognition and development of measures to address deficiencies in its legal system will benefit U.S. businesses operating in the Japanese market. Increasing the number of

Japanese lawyers will also help alleviate demands for legal expertise necessary for U.S. firms to successfully do business in Japan.

## **DISTRIBUTION AND CUSTOMS**

**Background:** The high cost of distributing goods from the point of entry to consumers has been a central irritant in our trade relations with Japan for many years. Although some progress has been achieved, more remains to be done. The introduction this year of new simplified customs clearance procedures and the new Large Scale Store Location Law mark important advances. However, the proposed introduction in October of a new fee structure for the clearance of air cargo may have a damaging impact on U.S. express carriers.

**Accomplishments:** Significant new Japanese measures include:

- Establishing a committee, which includes U.S. express carriers and other importers, to consider the impact of the proposed fee system reform for the clearance of air cargo. With this step, Japan has accepted a U.S. request that the interests of these carriers be taken into account when determining the final fee structure. The committee convened its first meeting on June 21, 2001.
- Implementing Simplified Declaration Procedures in March 2001. By this measure, Japanese Customs has taken a step towards the introduction of a paperless import clearance process. For established importers, the new regulations will provide streamlined procedures for duty payments and reporting requirements.
- Acting on its commitment to monitor the implementation of the new Large Scale Store Location Law (now in effect for one year) by local governments and to ensure that it is implemented in a consistent, transparent, and fair manner.
- Establishing guidelines for local governments to follow when administering the new Large Scale Store Location Law. Foreign and domestic retailers are still assessing the effect of the law to ensure that local issues relating to traffic, parking, etc. are not used to protect small shop owners at the expense of prospective large stores. In order to address these concerns, the Ministry of Economy, Trade and Industry has opened official contact "windows" in Tokyo and around the country which can help Large Scale Store market entrants.

**Benefits to the U.S.:** These measures will give U.S. express carriers a greater voice in the determination of possible fee increases that impact their business in Japan. The Simplified Declaration Procedures will benefit many established U.S. exporters to Japan. Reforms in the retail sector should give U.S. retailers greater access to Japan's \$1.5 trillion retail market.